Research Report

CAN FIN HOMES ANALYSIS

We have analyzed CAN FIN HOMES subject to some critical parameters as the stock has more than quadrupled in 2 -3 year time frame currently quoting at 1600 levels.

CAN FIN Homes is promoted by **CANARA BANK** operating in the NBFC segment catering services only to Housing Finance segment (HFC) which is the utmost Revenue driver for the company . The point here is the company has not diversified and has stuck to its guns.

Current Market cap of CAN FIN Homes is 5000 Cr (Approx.) There are a Numerous factors which is a big driver in the future for the NBFC segment, Housing for all by 2022, NPA well below the industry level of 0.70% Improving margins due to diversifying Cost of borrowing the percentage has come down from 8.99% to 8.75% depending lesser on banks to add sugar to lower cost borrowings. Cost to income ratio too being under 25% shows effective management

Management team:

CAN FIN Homes , MD Sharada Kumar Hota is from a Non-Banking background he is a Post Graduate in Agriculture science . The ratio of remuneration to the managing director to the employees of the company is 5.58: 1 , On March 2016 the company had 395 employees on Payroll .

The management has been so far excellent in terms of keeping the Asset quality under check and in terms of growth there has been a growth of 40% CAGR for 5 years. This shows the capital allocation skills of the management and seems to be good and par excellence with other companies in NBFC segment.

Growth:

Increase in the market share of NBFC from 26% in FY08-09 to 38% as of 2015, NBFC is having just a share of 13% in GDP compared to china at 26%. Smart cities, Growing Population and Middle income Group will be key drivers

Loan book growth @ 41.25% CAGR, Revenues 35.81% growth , PAT 30.18% , Net worth 23.47% CAGR for 5 years up to FY16 .

Revenues :

The company is primarily focusing on Loans in the Housing finance segment and the main customers are Salaried people 80% and Professionals 19% which makes the Loan book strong from recovery of loans, As most salaried people pay their dues in a Secured loan format unlike Credit cards which are Unsecured and Salaried may default about 88% are housing loans and 12% Non-housing loans . Geographically the company has 76% of loan sanctions in TN, AP, Telangana and Karnataka.

Asset Liability Structure:

This is a very important aspect in the lending business. The ratio to Assets and Liabilities maturing shows how well they are managed. The Asset sensitive bank or NBFC will enjoy higher NIM in a Interest rate Inclining environment and Vice versa for the Liability sensitive company. For Can fin homes for the 1 Year as on March 2016 Assets stand at 35352Lk and Liabilities at 97886Lk the ratio telling that 35322/97886 = 0.36 where the Maturity of liabilities(borrowings) is more than its assets(advances & investments) . This means the bank has to payout 97886 Lakhs worth borrowings with just 35322 worth advances and Investments maturing in 1 year period. Can Fin can be using Short term liabilities to fund Long term assets.

Valuations:

Current loan book estimated at 10640 Cr as of 2016 March , According to the reports of ICRA the housing credit sector has crossed 1.4 Trillion Rs as on Sept 15 , The sector witnessed an annualized growth of 17% in the HY 2015-2016 and the share of NBFC compared to banks in Home lending segments too have increased . Can fin homes is growing its Loan book at a CAGR of 41.25% CAGR which is way ahead of the industry growth of 17-20 %.

With a Conservative estimate of 25% in the next 5 years Loan book would be **32500 Cr** *(Company has given estimate around **35000 Cr**)* provided the NBFC has a good CAR at 20.69% higher than required level to grow in the future , The ability to raise capital through multiple sources like the NCD , NHB , Deposits etc. Currently on a 10643 Cr Loan book the NBFC earns a 9.8% Interest income of 1044.41 Cr and paid Interest of 743.48 Cr so total Net interest income being 300.93 with a NIM of 3.24% .

The average assets have grown at 24% for past 7 years, and estimating it to grow by 18% for next 5 years Average assets would be a little shy of 22000 cr and borrowings to have grown at 23% CAGR from 1966 Cr to 8401 Cr and after 5 years to be around 19200 cr at a CAGR of 18%

Current Yield on Assets is 11.24% and Cost of borrowing is 8.75%. so 5 years from now seeing a Constant Yield on assets we can estimate the Net interest received to be around 3315 Cr from 1044 Cr and Interest paid to be around 1680 Cr from 743 Cr , Thus Net Interest income would be around 2472- 1680 = 792 cr in 5 years from now.

Total interest received + Other income has grown at 26 % compared to the Interest paid at 25% which is more or less in line with the growth. Total Operating costs to be around 2472 Cr thus with a Operating income of 3315 -2472 = 850 Cr from current 273 Cr in 2022 .

Considering Provisions for NPA will remain at this level than on a 32500 Cr loan book with a GNPA of 0.25% = 81.25 crores after 5 years (A rough Estimate) .

From Operating Profits of 850 Cr we make a conservative estimate that nearly after 100% provisions than 80 cr to be written off and post taxes of 30% our Net profit in 5 years would be conservatively around 400 + Cr with EPS of 150 Per share with current Outstanding shares , Equity dilution is not estimated . Provisions can be higher or lower so more conservatively we approximate the Provisions to round of near 100 Cr (Provisions can be challenging to estimate)

Currently the stock is trading near 5 times BV (approx.) , with an ROE of 17.8% and a P/E of 28 times . Considering Returns on average assets (ROAA) to remain at 1.7 times than we can say that our earnings would be around 500 Cr. The stock with current multiples of 25 times would be around 3750 (without adjusting for split) at a 17% CAGR.

Consider this :

If I employ 1000 Rs in a Bank at 7% Interest = 70rs , my returns post a 30% tax would be ROE of 4.9% for a 1000 Rs deposit , So with a Bank or NBFC generating a 18% ROE than its justified to pay 3.6 times or 18/4.9 times BV . So thus value created will be 1000*18% = 180 with a 3.67 times book it will give the same 4.9% .

When I pay 5 times book than my returns shrink to 3.6% , This is why even though we have a positive outlook for the company in 5 years we are hesitant to pay the current price .

In this scenario Can fin homes seems to be trading little Overvalued at 5 times book. So the stock will look attractive at 1100 or below 1000 levels . Currently we will have it in our Watch list

Conclusion:

Its peers like PNB Housing, LIC HOUSING FINANCE all three being PSU are trading near 2.8 -3.5 times book. GRUH finance which trades at 12 times book (approx.) and HDFC which too commands a premium being the market leader. So even though the company has sound fundamentals we are skeptical to pay the price that the markets are demanding. In this scenario I would rather wait as Growth can be sluggish in terms of Loan growth due to currency issues, Interest rates can remain a catalyst, Realty sector is in a negative territory due to impacts on Macro factors. We remain mute with Can Fin Homes at current levels

This analysis is done by Ragavendhra Perumall, Independent Investor

Qualtrus (To be registered)

I have done this based on my understanding of the sector and financials. You can post your views, comments and if any discrepancies with the work at ragaav@yahoo.com

All data have been gathered in Annual reports of the company. Yields and Margins are calculated on assumptions as these may have a big variation going forward because 5 year period Interest rate cycles can change due to economic scenarios.

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